

REPORT OF THE AUDITOR-GENERAL TO THE WESTERN CAPE PROVINCIAL PARLIAMENT AND THE COUNCIL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE GEORGE MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2008

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the George Municipality which comprise the statement of financial position as at 30 June 2008, statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages xx to xx.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1, and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:
 - designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
 - selecting and applying appropriate accounting policies
 - making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3)(a) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing and *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance on whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.

6. An audit also includes evaluating the:
 - appropriateness of accounting policies used
 - reasonableness of accounting estimates made by management
 - overall presentation of the financial statements.
7. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the George Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.
8. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis of accounting

9. The municipality's policy is to prepare financial statements on the basis of accounting determined by the National Treasury, as set out in accounting policy note 1.

Basis for qualified opinion

Property, plant and equipment

10. Upon initial implementation of the Standards of Generally Accepted Municipal Accounting Practice, GAMAP 17 *Property, Plant and Equipment*, the municipality elected to make use of the transitional provisions in paragraph 86 of GAMAP 17 *Property, Plant and Equipment*, which allowed entities to delay the recognition of property, plant and equipment for three years following the date of first adoption.

As at 30 June 2008, the transitional provisions had lapsed and management was required to have fully recognised all property, plant and equipment in the statement of financial position. For the financial year under review, the exercise of fully recognising all property, plant and equipment had not yet been finalised. I was therefore unable to confirm or verify by alternative means the completeness of property, plant and equipment with a carrying value of R812,9 million, as disclosed in note 14 to the financial statements.

11. In terms of paragraph 56 of GAMAP 17 *Property, Plant and Equipment*, the depreciable amount of an item of property, plant and equipment is determined after deducting the residual value of the asset. Residual values were not determined for infrastructure, community and housing assets for the financial year under review. I was unable to confirm or verify by alternative means the accuracy of depreciation totalling R39,3 million, as disclosed in note 33 to the financial statements, and the valuation of property, plant and equipment with a carrying value of R812,9 million as disclosed in note 14 to the financial statements.

Employee benefits

12. During the financial year under review, the municipality opted for the early adoption of the South African Statements of Generally Accepted Accounting Practice, IAS 19 (AC 116) *Employee Benefits*, as reflected in accounting policy note 1. In terms of paragraphs 19 and 22 of GRAP 3 *Accounting Policies, Changes in Accounting Estimates and Errors*, the municipality had to retrospectively apply this change in accounting policy and restate the corresponding figures affected by the change in accounting policy.

The retrospective application of the early adoption of IAS 19 (AC 116) *Employee Benefits* was not performed, resulting in the entire defined benefit obligation of R62,4 million being recognised as a liability in the 2007-08 financial year, as disclosed in note 6 to the financial statements and expenses as disclosed in note 31 to the financial statements. The misstatement in the financial statements for the 2007-08 financial year and the prior financial periods is estimated at R55,9 million.

Qualified opinion

13. In my opinion, except for the effects of such adjustments, if any, as might have been determined to be necessary had I been able to satisfy myself as to the matters described in the Basis for qualified opinion paragraphs, the financial statements of the George Municipality as at 30 June 2008 and its financial performance and cash flows for the year then ended have been prepared, in all material respects, in accordance with the basis of accounting determined by the National Treasury, as set out in accounting policy note 1, and in the manner required by the MFMA and DoRA.

Emphasis of matters

I draw attention to the following matters:

Amendments to the applicable basis of accounting

14. As set out in accounting policy note 1, the National Treasury approved a deviation from the basis of accounting applicable to the municipality in terms of *General Notice 522 of 2007*, issued in *Government Gazette 30013* of 29 June 2007.

Casting errors in the financial statements

15. As disclosed in accounting policy note 2, the financial statements contain various casting, cross-casting and transfer differences. The municipality decided not to rectify these differences, as it considered the exercise to be time-consuming and that the benefit of reconciling rounding errors outweighed the cost to perform such an exercise.

OTHER MATTERS

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Internal controls

16. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Property, plant and equipment			■		■
Employee benefits		■	■		■

Control environment: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting.

Risk assessment: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives.

Control activities: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out.

Information and communication: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allows people to carry out their financial reporting duties.

Monitoring: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.

Non-compliance with applicable legislation

Municipal Systems Act

17. The human resources policies of the municipality did not provide a job description for each post on the staff establishment, as required by section 66(1)(b) of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA). Furthermore, the municipality's systems and procedures relating to personnel administration did not include the supervision and management of staff; the monitoring, measuring and evaluating of the performance of staff; the promotion and demotion of staff; the transfer of staff; and the dismissal and retrenchment of staff, as required by section 67(c), (d), (e), (f) and (j) of the MSA.

Matters of governance

18. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which I have assessed as follows:

Matter of governance	Yes	No
Audit committee		
• The municipality had an audit committee in operation throughout the financial year.	<input checked="" type="checkbox"/>	
• The audit committee operates in accordance with approved, written terms of reference.	<input checked="" type="checkbox"/>	
• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.	<input checked="" type="checkbox"/>	
Internal audit		
• The municipality had an internal audit function in operation throughout the financial year.	<input checked="" type="checkbox"/>	
• The internal audit function operates in terms of an approved internal audit plan.	<input checked="" type="checkbox"/>	
• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.	<input checked="" type="checkbox"/>	
Other matters of governance		
• The annual financial statements were submitted for audit as per the legislated deadlines in section 126 of the MFMA.	<input checked="" type="checkbox"/>	
• The financial statements submitted for audit were not subject to any material amendments resulting from the audit.		<input checked="" type="checkbox"/>

Matter of governance	Yes	No
• The annual report was submitted to the auditor for consideration prior to the date of the auditor's report.		■
• No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information.		■
• The prior year's external audit recommendations have been substantially implemented.	■	
Implementation of Standards of Generally Recognised Accounting Practice (GRAP)		
• The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007.	■	
• The municipality substantially complied with the implementation plan it submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP.		■
• The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008.	■	

Unaudited supplementary schedules

19. The supplementary information set out on pages xx to xx does not form part of the annual financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

OTHER REPORTING RESPONSIBILITIES

REPORT ON PERFORMANCE INFORMATION

20. I was engaged to review the performance information.

Responsibility of the accounting officer for the performance information

21. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

Responsibility of the Auditor-General

22. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
23. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
24. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

Non-compliance with regulatory requirements

25. The municipality has not developed and implemented mechanisms, systems and processes for the monitoring and review of, and reporting on, performance information, nor a structure for community participation, as required by the MSA and Local Government: Municipal Planning and Performance Management Regulations, 2001, issued in *GNR.796 of 24 August 2001*, resulting in various instances of non-compliance with the mentioned regulatory requirements, which can be summarised as follows:
 - (a) Key performance indicators did not include input and outcome indicators for each of the development priorities and objectives for the council's elected term, including its local economic development aims and its internal transformation needs, as required by section 9(1)(a) of the Local Government: Municipal Planning and Performance Management Regulations, 2001, issued in *GNR.796 of 24 August 2001*.
 - (b) Key performance indicators were not set for all employees and service providers, as required by section 9(2)(b) of the Local Government: Municipal Planning and Performance Management Regulations, 2001, issued in *GNR.796 of 24 August 2001* nor for all of the general key performance indicators prescribed in terms of section 43 of the MSA and set out in section 10 of the Local Government: Municipal Planning and Performance Management Regulations, 2001, issued in *GNR.796 of 24 August 2001*.
 - (c) The cost, resources and time used to produce outputs in accordance with the input indicators for each of the development priorities and objectives, referred to in section 26(c) of the MSA were not determined, as required by section 13(3) of the Local Government: Municipal Planning and Performance Management Regulations, 2001, issued in *GNR.796 of 24 August 2001*.

Performance information not received in time

26. I was not able to complete an evaluation of the quality of the reported performance information as set out on pages xx to xx of the annual report, since the information was not received in time.

OTHER REPORTS

Investigations

27. The municipality has initiated an investigation into alleged irregularities with regard to the execution of supply chain management regulations. The investigation aims to establish whether the initial appointment of contractors and the subsequent appointment of other contractors on an information technology project complied with legislative requirements and internal policies and procedures as well as to investigate the management of the project with specific emphasis on financial management. The investigation was still ongoing at the reporting date.

APPRECIATION

28. The assistance rendered by the staff of the George Municipality during the audit is sincerely appreciated.

Auditor - General

Cape Town

30 November 2008



A U D I T O R - G E N E R A L